Major Findings

This edition of *Performance Profiles* reviews financial and operating data for the calendar year 2005. Although the focus is on 2005 activities and results, it also discusses important trends prior to that time and emerging issues relevant to U.S. energy company operations.

Net Income and Profitability

- The Financial Reporting System (FRS) companies' 2005 net income increased 47 percent from the 2004 level to $119 billion, the highest net income (in constant dollars) in the history of the FRS survey. Higher prices for crude oil, natural gas, and petroleum products contributed to a 26-percent increase in operating revenues. Operating expenses also increased, by 24 percent, as higher prices stimulated exploration and development activities and pushed costs upward. The larger increase in revenues resulted in a 38-percent increase in operating income. The FRS companies earned a 28.2-percent return on stockholders' equity (ROE) in 2005, surpassing the previous peak of 22.1 percent in 2004. ROE for the FRS companies averaged 7 percentage points higher than that of the Census Bureau's All Manufacturing Companies from 2000 to 2005, reversing an average of 2 percentage points lower from 1985 to 1999.

- Higher crude oil and natural gas wellhead prices made oil and natural gas production the most profitable line of business for the FRS companies in 2005, providing $89 billion in net income and a return on net investment in place (ROI) of 24.5 percent. Earnings were $29 billion higher (in constant 2005 dollars) than the previous peak in 2004.

- Net income for the FRS companies' refining/marketing segment increased 30 percent from 2004, to $29 billion in 2005. Higher demand for petroleum products pushed prices up by more than the increased cost of crude oil. Domestic refinery operating and energy costs increased (on a per-barrel basis), but by less than the increase in the margin between petroleum product prices and crude oil prices. This resulted in a net refined product margin of $3.51 per barrel in 2005, the highest (in constant 2005 dollars) in the 29-year history of the FRS. The average ROI for domestic and foreign refining/marketing rose to 22.7 percent, also the highest in the history of the FRS survey.

Cash Flow and Uses of Cash

- Cash flow from operations increased in 2005 to $170 billion, the highest level reported since the FRS began collecting this information in 1986. Encouraged by the high-price environment in 2005, the FRS companies increased the amount of cash raised through disposals of assets by 82 percent over that raised in 2004, to $36 billion.

- The largest use of cash was for capital expenditures (measured as additions to investment in place), which increased by $46 billion from 2004, to $133 billion in 2005.

- FRS companies also increased the amount of cash used for non-investment activities in 2005. Dividends to shareholders were the second largest use of cash, increasing 9 percent, to $40 billion. The largest increase on a percentage basis in use of cash was to buyback company stock, which more than doubled to $32 billion in 2005.

- The large increase in cash flow also reduced the need for long-term debt financing. FRS companies increased the amount of cash used to reduce long-term debt by 81 percent in 2005 to $33 billion. Proceeds from issuing long-term debt also increased, but by a smaller amount. Overall, the ratio of long-term debt to stockholders' equity for FRS companies fell 8 percentage points in 2005 to 37.3 percent, the lowest level since 1983.

- The overall uses of cash did not keep pace with increases in sources of cash, resulting in an increase in cash balances and cash equivalents of $14 billion in 2005. Although this was less than the 2004 increase, it was the second-highest annual addition to cash balances in the 20 years the FRS has been collecting cash flow information.

E&P Expenditures

- FRS companies report expenditures for exploration, unproved property acquisition, development, proved property acquisition, and production (E&P) for the oil and natural gas production segment. FRS companies were hesitant to increase investments in response to higher cash flow in 2003 and 2004, but in 2005 the increase in E&P expenditures exceeded the increase in cash flow from operations by $10 billion. E&P expenditures increased $39 billion (in constant 2005 dollars) over their 2004 level to $131 billion in 2005. Expenditures for unproved and proved property acquisition accounted for 55 percent of the increase in E&P expenditures, as several large acquisitions occurred.

- Worldwide expenditures for oil and natural gas exploration (not including expenditures for unproved property) by FRS companies increased 21 percent (in constant 2005 dollars) to $10 billion in 2005, but remained well below the levels of the early 1980s. Development expenditures rose 27 percent from 2004 to $50 billion in 2005, the highest level in the history of the FRS survey.

Refining/Marketing Capital Expenditures

- Capital expenditures by the FRS companies for refining and marketing increased 49 percent from their 2004 level to $21 billion in 2005, mostly as the result of mergers and acquisitions. Several companies reported refining/marketing capital expenditures to meet more stringent specifications for petroleum products and to enhance their capability to process heavier crude oil and produce more light products. Expenditures were also required to repair damage from hurricanes.

Oil Production and Reserves

- The FRS companies' worldwide production of oil (crude oil and natural gas liquids [NGL] combined) and natural gas both declined by more than 3 percent in 2005. U.S. offshore production fell substantially, attributable largely to Hurricanes Katrina and Rita. U.S. production of oil by FRS companies declined 7 percent in 2005 and U.S. natural gas production fell 5 percent. Foreign production by FRS companies also declined, by about 1 percent for both oil and natural gas.

- FRS companies' reserve additions through drilling (i.e., excluding purchases and sales of reserves) increased significantly from their low level in 2004, to 5.5 billion barrels in 2005. Reserve revisions of oil rebounded from a large negative position in 2004 to become net positive in 2005.

- The FRS companies' reserve replacement rate for natural gas (averaged over 3 years) has risen steadily for the past several years, reaching 123 percent in 2003-2005 period. Conversely, the reserve replacement rate for oil fell substantially in the 2002-2004 period and declined slightly more in the 2003-2005 period to 63 percent.

- In 2005, the FRS companies accounted for 45 percent of total U.S. crude oil and NGL production and 43 percent of U.S. natural gas production, both having declined slowly over the past several years. FRS companies had 49 percent of U.S. crude oil and NGL proved reserves in 2005 as well as 49 percent of U.S. natural gas reserves. While this was the first year that the FRS share of oil reserves fell below 50 percent, the FRS share of natural gas reserves has increased the past two years.

Finding and Lifting Costs

- Average worldwide finding costs for FRS companies increased 17 percent in the 2003-2005 period relative to the 2002-2004 period, to $10.73 per barrel of oil equivalent (boe), as high demand for drilling rigs and personnel put upward pressure on costs. Finding costs in the U.S. offshore increased by 55 percent, due in large part to lower reserve replacement in the 2003-2005 period relative to the 2002-2004 period, which was partly attributable to damage and delays from hurricanes in 2005. Finding costs declined 7 percent in the U.S. onshore region, but rose 42 percent in foreign regions. Lifting (production) costs increased in every FRS region except one, to an average of $6.87 per boe in 2005. Finding and lifting costs combined increased to $16.89 per boe in 2003-2005, the highest since the 1985-1987 period (in constant dollars).